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IN THE

United States

Circuit Court of Appeals,

FOR THE NINTH CIRCUIT.

Gary Swan,
Plaintiff and Appellant,
vs.
Consolidated Water Company of Pomona, etc., et al.,
Defendants and Appellees.

APPELLEES' REPLY BRIEF.

KEMPER CAMPBELL,
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Parker, Stone & Baird Co., Law Printers, Los Angeles.

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APPELLEES' REPLY BRIEF.

Plaintiff and appellant has appealed from an order dismissing this action for want of jurisdiction and insufficiency of fact to constitute a valid cause of action in equity. [Tr. p. 18.]

Both grounds of objection were argued before the trial court and extensive briefs submitted thereon.

Want of Jurisdiction.

The bill of complaint should be dismissed on the ground that Swan was collusively made plaintiff "for the purpose of creating a case cognizable" in the United States District Court.

Jud. Code, Sec. 37;

Montgomery's Manual, Third Ed., Sec. 91; Sec. 764, 765;

Laughner v. Schnell, 260 Fed. 396, 397.

It is true that there are cases which seem to indicate that the courts have held with respect to stockholders' bills that a suit need not necessarily be deemed collusive in respect to the party plaintiff if the suit is brought by the plaintiff in good faith to protect his own individual right, even though others may join in paying the expenses.

Hutchinson Box Board & Paper Co. v. Van Horn, 299 Fed. 424.

In the Hutchinson case the foreign plaintiff was actually contemplating the bringing of a suit prior to any negotiation with other stockholders or their representatives, and ultimately actually authorized the institution of such suit. The plaintiff appeared at the trial, testified as witness and was actively connected with the entire litigation. It will be noted that there is a strong dissenting opinion in the Hutchinson case, in which the case of Cashman v. Amador & Sacramento Canal Co., 118 U. S. 58, 30 L. Ed. 72, is cited, and it is stated that the same "has never been modified."

The case at bar comes within the reasoning of the Cashman case. As there held, the "dispute or controversy" was "really and substantially" one between a county and citizens of the same state, and "the suit was originally brought by the county of Sacramento for its own benefit" and was carried on at its sole charge, while "the name of Cashman was used with his consent" as that of a mere nonresident landowner, "because the county could not sue in its own name" in the federal court. It was the suit of the county with a party plaintiff "collusively made," and "for the purpose of creating

a case cognizable" by that court, and thus within the Act of March 3, 1875, 18 Stat. 470, c. 137 (U. S. Comp. St. 1901, p. 511, Sec. 5).

The case at bar is even a stronger one in favor of defendants than the Cashman case in that it appears that not only was the plaintiff chosen by Stillwell and his attorney as the nominal plaintiff, but the plaintiff has not consented to act as such nor has he authorized the bringing of a suit. The testimony of Stillwell and Austin [Supplement to Transcript of Record] shows a most unusual and astonishing state of affairs and a manipulation by which it was hoped to invoke the jurisdiction of this court and which serves to distinguish this case from any decisions which the appellee has been able to discover involving the question submitted upon this motion.

The story in brief, as revealed by this testimony, is that J. E. Stillwell has a relative by marriage who happened to be one of the legatees under the will of Emily Brady Gridley, deceased, J. E. Stillwell and defendant G. A. Lathrop being co-executors of said will. The legatee was bequeathed shares of stock in defendant, Consolidated Water Company, but Stillwell's relative "thought he ought to have his share of the money" [Supplement to Transcript, p. 3], and Stillwell then interested himself in an endeavor (using the language of the lower court) "to get the cash for legatees who were, as a matter of law, entitled to the stock," * * * while, "as a matter of law, his business was to distribute the stock." [Supplement to Tr., p. 11.]

Having discovered there was a man by the name of Swan who owned some sixty-five shares out of the five

thousand shares issued, he wrote to Mr. Swan telling him "that Mr. Austin would take the proposition on a contingent fee, if he wished to join, and he wired back that he would like to do so." [Supplement to Tr., p. 6.]

We find no testimony in this record which indicates that Swan ever authorized the bringing of this suit. It will be noted that the bill is verified by Mr. Austin and not by Swan. It affirmatively appears from the testimony that Swan did not authorize the bringing of the suit. It will be noted that the real actor in this whole matter is Stillwell who not only desired in some way to liquidate the holding of his wife's brother-in-law but also desired to receive a split on the attorney's fee which probably has added to his zeal in this matter. [Supplement to Tr. p. 17; Tr. p. 18, lines 26, *et seq.*]

If Your Honors will read the examination of Mr. Stillwell by Mr. Austin [Supp. to Tr., pp. 17, 18]—and between the two of them the real facts are revealed—it will conclusively appear that this suit was filed without any authorization whatever by Swan and that Swan was chosen by Stillwell and Austin for the sole and collusive purpose of conferring jurisdiction upon this court in a matter which should be tried, if at all, in the state court. In response to questions by his own counsel, he admits that nothing was said in his correspondence about the means to be employed "or what the relations of the parties might be" but that "it was just simply to employ Mr. Austin to look after his interests." When Stillwell's attention was called to his previous testimony mentioning the possibility of a suit, he said [Supplement to Tr., p. 14]:

"A. Well, I did not think a suit would be necessary, until he said the code didn't provide for the dissolution under those circumstances—I never supposed a suit would be necessary to distribute this money.

"Q. That was after you had heard from Mr. Swan, wasn't it?

"* * * Well, it must have been afterwards" etc.

Attorney for plaintiff later on brings out from Stillwell his efforts to effect a voluntary dissolution purporting to represent Swan in this attempt. [Supplement to Tr., pp. 18, 19]. The date of the Swan correspondence is placed in June or July, 1927. These efforts in behalf of Swan for voluntary dissolution are dated August 31 and thereafter.

It is further shown that before the suit was brought a number of local stockholders were solicited as clients in this matter by Mr. Stillwell and after these other stockholders were induced to become clients, and all of them residents of California, Swan, who was a nonresident, was deliberately chosen to act as the nominal plaintiff without any authority whatever on the part of Swan so to do. We believe that this is not a situation where a plaintiff is in good faith desirous of prosecuting a suit and is himself here seeking to do so. It appears without controversy that Swan was importuned. Stillwell testified [Supplement to Tr., p. 6]:

"I wrote to Mr. Swan and told him that Mr. Austin would take the proposition on a contingent fee, if he wished to join, and he wired back that he would like to do so."

"To join" whom? Apparently to join others who were interested in a *voluntary* dissolution of a corporation or to join with others in employing Mr. Austin to liquidate the stock, by negotiation and not by suit, because as Mr. Stillwell says, "I never supposed a suit would be necessary to distribute this money," and, as Mr. Austin brings out, Stillwell "simply suggested to him (Swan) that he should employ an attorney" and nothing was said about the bringing of a suit or "type of an action" required.

The reporter has added to the transcript and same has been inserted as pp. 20 and 21 thereof, the statement of Mr. Austin. This statement sets the matter at rest beyond question. He says:

> "I was employed by Mr. Swan some time along in July, I believe it is—it may have been August, 1927—to make an effort on his behalf to secure a dissolution of the Consolidated Water Company of Pomona, and to secure a distribution to its stockholders, particularly to himself, of his proportionate share of its assets. At the time of that employment there *was no discussion or determination of just what steps would be taken. At that time I had not determined what steps would be taken,* but I anticipated that it *might be brought about by friendly negotiations; and pursuant to that employment I undertook such negotiations,* and *I* then began to cast about to determine what kind of an action to bring and where to bring it, in order to produce the best results. And the present suit is the result of that consideration on my behalf."

There is no intimation that Swan at the time of the employment anticipated a suit, it clearly appears that his attorney did not, and there is no indication that

Swan either authorized or knew anything about, or yet knows anything about the filing of this suit.

So we have in this case, differentiating it from those cases where suit is allowed, the fact that this suit is not only brought in behalf of the corporation which is a California corporation, but all of the other stockholders are residents of California, the attorney for plaintiff is also attorney for a number of other resident stockholders, and has actually appeared for them in the action—thus representing both plaintiff and defendants, the fact that attorney for plaintiff represented at least some of these nominal defendants prior to the institution of the action and the fact that Stillwell had guaranteed the costs of the suit so that counsel was at liberty to bring the action in the name of any of the other parties whom he represented and who were residents of California and the fact that he was not definitely authorized by plaintiff Swan to bring the action nor was any suit contemplated by Swan or by Stillwell when Austin was employed, nor has any subsequent authorization to bring this suit been had.

Collusion within the meaning of the statute (Judicial Code, sec. 37) has been proven. The real party in interest, and the party for whose benefit this suit is brought, is the corporation. As will later be shown, no stockholder, as an individual, has a right to have awarded to him a portion of the assets of the corporation, and therefore this suit is merely a stockholder's bill brought for the benefit of the corporation.

As stated by Judge Montgomery in his Manual, on page 73:

"As to whether the case is within the scope of its jurisdiction, is a question which the court is bound to examine and determine, although not presented by the parties,—and even where they consent to a determination of the controversy on its merits. 'Consent cannot confer jurisdiction, and want of jurisdiction cannot be waived.' The same obligation rests upon a reviewing court; and on every writ of error or appeal, the preliminary inquiry is as to the jurisdiction (1) of the appellate court, and (2) of the court from which the record comes. And, inasmuch as a federal court is a court of limited jurisdiction, the fact that the case is one of which the court may take cognizance must appear affirmatively from the record,—otherwise a reversal must be ordered.

"Unless the contrary affirmatively appears, a presumption will be indulged that a cause is not within the court's jurisdiction."

O'Neil v. Co-operative League of America, 278 Fed. 737.

Insufficiency of Fact to Constitute a Valid Cause of Action in Equity.

As indicated by the title of the bill, the suit is "for dissolution of corporation and for a receiver." Consolidated Water Company of Pomona is a California Corporation. The matter is governed by the law of the state of California. Sections 564 and 565 of the Code of Civil Procedure and the decisions of the Supreme Court of California applying these provisions are determinative against plaintiff's bill. These sections are as follows:

"Sec. 564. Appointment of receivers. A receiver may be appointed by the court in which an action is pending, or by the judge thereof.

"1. In an action by a vendor to vacate a fraudulent purchase of property, or by a creditor to subject any property or fund to his claim, or between partners or others jointly owning or interested in any property or fund, on the application of the plaintiff, or of any party whose right to or interest in the property or fund, or the proceeds thereof, is probable, and where it is shown that the property or fund is in danger of being lost, removed, or materially injured;

"2. In an action by a mortgagee for the foreclosure of his mortgage and sale of the mortgaged property, where it appears that the mortgaged property is in danger of being lost, removed, or materially injured, or that the condition of the mortgage has not been performed, and that the property is probably insufficient to discharge the mortgage debt;

"3. After judgment, to carry the judgment into effect;

"4. After judgment, to dispose of the property according to the judgment, or to preserve it during the pendency of an appeal, or in proceedings in aid of execution, when an execution has been returned unsatisfied, or when the judgment debtor refuses to apply his property in satisfaction of the judgment;

"5. In the cases when a corporation has been dissolved, or is insolvent, or in imminent danger of insolvency, or has forfeited its corporate rights;

"6. In an action of unlawful detainer, in those cases in which the Superior Court has exclusive original jurisdiction;

"7. In all other cases where receivers have heretofore been appointed by the usages of courts of equity. (Amendment approved May 3, 1919; Stats. 1919, p. 251.)"

"Sec. 565. Appointment of receivers upon dissolution of corporations. Upon the dissolution of any corporation, the Superior Court of the county in which the corporation carries on its business or has its principal place of business, on application of any creditor of the corporation, or of any stockholder or member thereof, may appoint one or more persons to be receivers or trustees of the corporation, to take charge of the estate and effects thereof and to collect the debts and property due and belonging to the corporation, and to pay the outstanding debts thereof, and to divide the moneys and other property that shall remain over among the stockholders or members. (Amendment approved 1880; Code Amdts. 1880, p. 4.)"

It will be seen that there is no provision for the appointment of a receiver which by any possible construction of the bill of complaint is applicable here. Subdivisions 1, 2, 3, 4 and 6 of sec. 564 are obviously outside the scope of the bill and as to subdivision 5, the corporation must have already been "dissolved" or "insolvent" or "in imminent danger of insolvency" or "has forfeited its corporate rights." There is no such allegation in the bill.

As to subdivision 7, the Supreme Court of this state has in no uncertain terms eliminated it from any pertinency to this case. (See authorities hereinafter cited.)

As to sec. 565, the language "upon dissolution" has been construed to mean "*after* dissolution." (Henderson v. Palmer Union Oil Co., 29 Cal. App. 451 at p. 458.)

That there is no ground presented for dissolution will appear also from authorities hereinafter quoted for the court's convenience.

Elliott v. Superior Court, 168 Cal. 727, 728, 730-733:

> "At the time it filed its complaint the plaintiff moved the court for an order appointing a receiver of the assets of the defendant for the benefit of itself and all other persons similarly situated. The grounds of the motion were 'that the plaintiff has no adequate remedy at law, and that the funds out of which the plaintiff and other creditors must look for the payment of their claims is in danger of waste, loss and destruction.'
>
> "The order appointing the receiver is void and all of his acts performed in pursuance of his illegal appointment are necessarily void. Section 305 of the Civil Code, found in title I, part IV of that code, and which title contains provisions applicable to all corporations formed under the laws of this state, provides: 'The corporate powers, business, and property of all corporations formed under this title *must be exercised, conducted and controlled* by a board of not less than three directors.' The court, through the appointment of a receiver, exercises the powers, conducts the business and controls the property of the corporation, which by virtue of this section, can only be exercised, conducted, and controlled by a board of directors. There is no law of this state, nor can any decision of our Supreme Court be found, which authorizes a court, through a receiver, to take charge of the business and property of a corporation before dissolution, dispose of its assets and wind up its affairs. On the contrary, this court has repeatedly and consistently held for more than fifty years last past that the courts have no jurisdiction to appoint a receiver of the entire

assets of a corporation in a suit prosecuted by a private party. (Neall v. Hill, 16 Cal. 151; 76 Pac. 508—French Bank Case, 53 Cal. 495—Smith v. Superior Court, 97 Cal. 348; 32 Pac. 322—Smith v. Los Angeles and P. R. Co., 4 Cal. Unrep. 237; 34 Pac. 242—Murray v. Superior Court, 129 Cal. 628; 62 Pac. 191—Fischer v. Superior Court, 110 Cal. 129; 42 Pac. 561.) * * *

"* * * A corporation cannot in this indirect manner destroy itself. It cannot put beyond its reach the power to do that for which it was created. It is the creature of the law and its powers must be exercised in the manner prescribed by law and not otherwise. If it wishes to die, it may do so, but only in the way ordained by law. It must first satisfy and discharge all claims and demands against it; two-thirds of its members or stockholders must resolve upon dissolution and the provisions of title VI, part III of the Code of Civil Procedure relating to the voluntary dissolution of corporations must be complied with. If it must be put to death against its will, then the state and not a private party must institute proceedings with that object in view. In Smith v. Superior Court (97 Cal. 348; 32 Pac. 322), this court was asked to review an order of the Superior Court of Los Angeles county appointing a receiver in an action brought by the California Bank against the Los Angeles and P. R. Company to recover judgment upon an unsecured promissory note. As in the case now under consideration, the plaintiff in that case applied for and the defendant consented to the appointment of a receiver and the court made the appointment. Yet this court held that the order appointing the receiver was void and in excess of the jurisdiction of the Superior Court. * * * "

The leading case, and one which has been repeatedly followed, is French Bank Case, 53 Cal. 495, 550-554:

> "The case here not being *in error* but upon *certiorari*, the inquiry is of course to be confined to a consideration of the *mere power* of the district court to *appoint a receiver* in a case of this impression.
>
> "Irrespective of the effect of the fifth subdivision of sec. 564 of the Code of Civil Procedure, which will be presently considered, there is no jurisdiction vested in courts of equity to appoint a receiver of the property of a corporation in a suit prosecuted by a private party. This is only to say that there is no jurisdiction vested in these courts in such a case to dissolve a corporation; for the power of a receiver, when put in motion, of necessity supersedes the corporate power. It necessarily displaces the corporate management and substitutes its own, and assumes, in the language of the order under review, 'to do all and everything necessary (in the judgment of the receiver, under the advice of the court) to protect the rights of the creditors and depositors of said corporation.'
>
> "'This precise question was brought directly under consideration here in the case of Neall v. Hill, 16 Cal. 145, where, in a suit brought by a stockholder, a receiver had been appointed by the district court to take possession of the property of the 'Gold Hill and Bear River Water Company,' a corporation existing under the laws of this state. The opinion in that case, rendered by Mr. Justice Cope, and concurred in by the whole court, after referring to the adjudicated cases in England and in this country, uses this language: 'This decree, if permitted to stand, must necessarily result in the dissolution of the corporation; and in that event the

court will have accomplished, in an indirect mode, that which, in this proceeding, it had no authority to do directly. It is well settled that a court of equity, as such, has no jurisdiction over corporate bodies for the purpose of restraining their operations, or winding up their concerns. We do not find that any such power has ever been exercised in the absence of a statute conferring the jurisdiction.'

* * * * * * * *

"We proceed, therefore, to inquire whether the jurisdiction of the courts of equity, in the respect referred to, has been enlarged by any statute of this state. The only statute brought to our attention, which is supposed to have that effect, is sec. 564 of the Code of Civil Procedure.

* * * * * * * *

"That the case brought into the District Court of the Fifteenth Judicial District is not included in the sixth subdivision of this statute has been determined already; and the appointment here not having been made 'after judgment,' of course the third and fourth subdivisions can have no application. The first and second subdivisions provide for the appointment of a receiver in an action brought by a vendor to vacate a fraudulent purchase; in aid of a creditor's bill; also, in proceedings involving questions between partners; also, in suits of foreclosure brought by mortgagees when the security is likely to be lost or seriously impaired. These subdivisions do not assume to create a substantive right of action where none existed before. Their aim is to provide a more efficacious remedy in the conduct of actions, the right to bring which already exists, and are elsewhere provided for. The action by a vendor to vacate a fraudulent purchase, or by mort-

gagee to foreclose a mortgage, is not created by the statute we are now considering—they exist independently of its provisions, and would continue to exist if this statute were repealed.

* * * * * * * *

"We are, therefore, of opinion that the said orders of October 7, 1878, assuming to appoint a receiver in the case of Thomas J. Gallagher v. L. A. Societe Francaise d'Epargnes et de Prevoyance Mutuelle, were in excess of the jurisdiction of the district court, and that they be annulled. So ordered."

Fischer v. Superior Court, 110 Cal. 129, 140-142.

"In Neall v. Hill, *supra*, where a receiver had been appointed to take possession of the property of a corporation, the court said: 'It is well settled that a court of equity, as such, has no jurisdiction over corporate bodies for the purpose of restraining their operations or winding up their concerns. We do not find that any such power has ever been exercised in the absence of a statute conferring the jurisdiction.' * * * The general authorities on the subject are to the same effect. Beach on Receivers, section 403, speaking of receivers of corporations, says: 'It is, in the first place, to be remarked that the jurisdiction to appoint a receiver in these cases is wholly statutory.' The question to be determined, therefore, is whether or not there is any statutory provision under which power is given a court to appoint a receiver in a case like the one at bar during the pendency of the suit.

* * * * * * * *

"It is difficult to understand upon what ground the right to a receivership is based in the case at bar, or what that position is which, it is contended, lifts the plaintiff in the case above the principles

hereinbefore stated, and enables him, through the agency of a receiver, to take from a corporation the management of its affairs, during the pendency of an action."

"Upon dissolution," as used in C. C. P. 565, means *after* dissolution has been decreed.

Henderson v. Palmer Union Oil Company, 29 Cal. App. 451, 458:

"It is at least perfectly clear that 'upon dissolution' does not mean 'before dissolution.' The phrase undoubtedly means 'after dissolution,' and it is not limited to any particular lapse of time. It may include an application made immediately following the dissolution or one separated by quite a period of time.

"Of course, after dissolution the corporation is not 'alive,' and it is not strictly accurate to say that it has a place of business. But if the section is to have any application at all, it must be in a case of dissolution, as by no possible construction can it refer to the appointment of a receiver for a going concern."

It is only in a case where the directors are in jail, or have wholly abandoned their trust, and the corporation is not doing business, that a receiver may be appointed. (California Fruit Growers' Association v. Superior Court, 8 Cal. App. 711, 712.)

If directors are not conducting the business lawfully, the remedy is by injunction. (Dabney Oil Co. v. Providence Oil Co., 22 Cal. App. 233, 237-239.)

As stated in the case of Lyon v. Carpenters' Hall Assn., 66 Cal. App. 550, 552:

> "If Carpenters' Hall Association (a corporation) had suffered no forfeiture, or if it had not been dissolved, the courts would have no right through a receiver to take possession of the corporation's property, to sell the property, or to distribute the proceeds among the persons entitled thereto, because the law has placed all of those powers in the hands of the directors of the corporation. (Civ. Code, sec. 305.)"

There is no case cited by counsel in which a court has granted a receiver under circumstances as set forth in this case because some impatient stockholder employs over-zealous counsel to file a suit.

It would be a very disastrous state of affairs, one which would bring calamity upon the business of this nation, if any dissatisfied stockholder, under the facts alleged in this bill, could come in and demand the destruction of the corporation, or what amounts to a wrecking of it by putting it into the hands of a receiver.

California Statutes and Decisions Have Established a Rule of Property by Limiting Dissolution of Corporations. Rules of Property So Established Will Be Respected by the Federal Courts.

Corporations are the mere creatures of the statute. The state has the exclusive power to create them, to measure the rights, liabilities, privileges, immunities and responsibilities of these artificial entities and of their stockholders. When stock is acquired in the state of California, the purchaser has a right to rely upon the fact that the corporation in which stock is acquired will exist for fifty years, for the period designated in the franchise or by statute, and that it cannot be dissolved

"* * * this court has deferred to decisions of the state courts, even in cases where those decisions were not expressive of public policy or declaratory of a rule of property. Columbia Digger Co. v. Sparks, 227 F. 780, 142 C. C. A. 304; American Surety Co. v. Bellingham Nat. Bank, 254 F. 54, 165 C. C. A. 464."

The court declared further that:

"'Broadly speaking, the rule is that when the decision in a federal court involves no federal question, the case being there solely by reason of diversity of citizenship, and when the law invoked, whether common law or statutory law, is of local character, and has become established as a part of the law of the state, a federal court will follow the decisions of the state court of last resort when decisions of that court exist.' So in Sturtevant Co. v. Fidelity & Deposit Co., 285 F. 367, the Circuit Court of Appeals for the Second Circuit, in dealing with a bond given by a school contractor, said: 'Although the question is one of general law * * * yet, under well-settled principles, this court should, if possible, be in harmony with the New York courts in respect of a question of this character.'

"From the foregoing considerations we reach the conclusion that, in determining the rights of litigants arising out of a contract of suretyship such as this, made and to be performed in the state of Washington, a federal court should follow the rule established by the highest court of that state."

In the case of *T. L. Smith Co. v. Orr,* 224 Fed. 71 (C. C. A. 8), decision by Judge Sanborn, it is held:

"The question is whether or not a receiver appointed in a creditors' suit in Missouri to administer

> and convert into money the property of an insolvent debtor, and to distribute the proceeds thereof among its creditors, has the right and power to avoid an unrecorded condition of a contract of conditional sale which the creditors might have disregarded if no receiver had been appointed. This is a question of local law, of the construction of a statute of Missouri, and of the determination of the judicial practice under it in that state, and if there were a decision of this question by the highest judicial tribunal of that state it would be controlling in the federai courts. No such decision, however, has been cited or found, but the following rules of law and practice seem to prevail in the courts of that state * * * "

This language is followed by an analysis of the decisions of the statutes of the state of Missouri, which decisions and statutes the court endeavors to follow.

If the powers of a receiver are limited by the laws of the state in which he is appointed, it surely follows as a matter of course that the appointment of the receiver in the first instance is limited by the laws of that state. It would be a grotesque situation if a federal court could appoint a receiver contrary to the provisions of local law and allow him to reach out and grasp the property of the corporation itself, and thereupon be required to circumscribe his handling of the property in accordance with local laws.

In the case of *Zacher v. Fidelity Trust, etc. Co.,* 106 Fed. 593 (9 C. C. A. 6), decision by Judge Lurton, it is held:

> "Where the question is as to the validity of a particular foreign assignment under the law of

> Kentucky, we ought not to hesitate to yield to the authority of the highest court of that state, when we find that upon an identical record between the same parties it has held the assignment in question not such a voluntary assignment as by the comity of that state is valid as against the subsequent lien of local creditors. The decision of the Kentucky court is one of blended law and fact, and so far concerns the purely local policy of that state that we are not disposed to refine in respect to how far we might reach a different conclusion upon the same facts and yet administer the law of the state. It would be a scandal upon the administration of justice if two co-ordinate courts, administering the same law, should reach a different conclusion upon the same facts; and more especially would this be so in respect of a matter in which the highest court of the state whose comity and policy was involved had led the way by a decision between the same parties in respect to another fund embraced in the same assignment."

In the case of *Loewe v. California State Federation of Labor, et al.*, 189 Fed. 714, Judge Van Fleet concedes that "in the administration of their equitable jurisdiction" the federal courts are bound by "local statutes," and even in the absence of local statutes, the reasoning of a state court "is always to be regarded with respect, and will be followed, if persuasive of a correct statement of the law," although not absolutely binding.

We have here under consideration all of these factors, to-wit: (1) A rule of property; (2) local statutes; and (3) persuasive decisions of the Supreme Court of California.

Appellant cites a number of cases wherein receivers have been appointed for *insolvent* corporations. These decisions do not aid appellant, for the reason that it is conceded that where a defendant corporation is insolvent a stockholder or creditor would be entitled to have a receiver appointed, under section 564 of the Code of Civil Procedure of California. Most of the authorities cited by plaintiff are of this character, and the others are readily distinguishable from the case at bar. In other words, the position of appellees is that even if the court were not circumscribed by the statutes of California, and this were not a case of a rule of property, the court, in the exercise of its general equity jurisdiction would not under the allegations of this bill grant a receiver, nor would it entertain an action for the dissolution of the corporation.

We refer briefly and *seriatim* to the authorities cited by appellant:

Cramer v. Bird, 6 L. R. Eq. 143.

This case is an English case decided in the year 1868. The company had ceased to carry on its business, the directors had rendered no account and declared no dividends and no meeting of the shareholders had been held since the passage of the last Act concerning the corporation.

Enterprise Printing & Publishing Co. v. Craig, 135 N. E. 189 (App. Ct. of Indiana, Div. 2).

This is an isolated case in which the state court of Indiana has admittedly gone farther than perhaps any other court in the United States, in an endeavor to adjust a difficulty between a stockholder who owned 480 shares

as against other stockholders who owned 520 shares. There was apparently no right of cumulative voting, and plaintiff Craig in that case could not elect himself to the board of directors, and he desired participation in the business. The situation was more in the nature of a partnership in corporate form, Craig owning 480 shares and the Neal family owning 520 shares. The bill in that case showed that the Neal family had fixed exorbitant salaries for themselves, absorbing the profits of the corporation, and had indulged in a long series of misappropriation and embezzlements of corporate funds and properties. In the Craig case it was shown also that the books of the corporation were so kept as to conceal numerous fraudulent financial transactions, and that stockholder Craig was not permitted the right to examine the books. It appears that there was no trouble in the Enterprise Printing & Publishing Company so long as Craig was allowed to be on the board of directors. In California, the minority is protected by the law giving the right to cumulate the shares and vote the entire amount for one or any other proportionate number of directors, as the case may be.

It will readily be seen that a number of factors are present in the Enterprise case that are not present in the case at bar. In the case at bar the minority under the law has the right to elect its proportionate number of directors, the stockholders are at perfect liberty to examine the books and audit them, no fraud has been charged in the bill, salaries have not absorbed the profits, nor are there any falsifications of records or any concealment of any kind. On the contrary, the operation of the corporation under the management of Lathrop

has been exceedingly profitable. The value of the stock has increased from almost nothing to $120.00 per share.

Exchange Bank of Wewoka v. Samuel Bailey, 26 Oklahoma 246; 116 Pac. 812.

In this case, it was alleged that no certificate or statement of condition of the affairs of the bank was made or rendered and that the president and the cashier of the bank refused to make a statement of the business of the bank for over a year, or of the profits; that the officers and directors complained of refused to permit plaintiff to participate in the control of the business or permit him to examine and ascertain for himself the condition of the books. The court said:

> "If such acts do not constitute fraud they, at least, constitute such gross mismanagement, *the bank being insolvent,* as to justify a court of equity in reaching out its arm and protecting the minority stockholders and the creditors of the bank by placing the assets of the bank in the hands of a receiver."

This case is distinguished from the present case in that the corporation was insolvent.

Fougeray v. Cord, 50 N. J. Eq. 185; 24 Atlantic 499.

In this case, it was alleged that the plaintiff and two associates entered into an agreement to subdivide and sell a farm. The plaintiff complains that his two associates elected themselves directors, sold the farm at a profit of $37,000.00 and paid themselves salaries of $16,000.00, whereupon they organized another company and turned over the assets to the other company. After the filing

of this Bill in Equity, they returned the assets, but the court held that the plaintiff was entitled to his relief in spite of this attempted restitution. It will be readily seen that the facts in the above case have no bearing upon the case before this court.

We have hereinbefore adverted to the *French Bank Case,* 53 Calif. 495.

Klugh v. Coronaca Milg. Co., 66 S. Car. 100; 44 S. E. 566.

This case was decided by the court of South Carolina, and it was held that under the law of that state a minority stockholder had the right to bring an action to wind up the business of the corporation upon a showing of fraudulent acts, *ultra vires* acts, negligence of directors, and a request to the corporation to correct the alleged wrongs.

A decision from South Carolina would have no bearing upon this case, in view of the consistent and well-settled law of this state in regard to the dissolution of corporations.

Merchants Line v. Wagner, 71 Ala. 581.

The holding in this case was directly opposite to the contentions made by the appellant. The court said:

> "Very true, the bill charges that three, a majority of the directors, have combined and formed a ring for their own private profit, at the expense of the other stockholders, and many acts of wrong doing are charged against these three directors. No act is charged that is *ultra vires,* and there is no averment that the corporation's assets are imperiled by the insolvency of the parties."

The term for which the corporation was incorporated had expired and the venture was continued by common consent. The court held that, considered as a bill to settle the accounts of a dissolved corporation, the action could be maintained, but that it stated no grounds for the dissolution of a corporation previous to the natural expiration of the term which had been agreed upon by the incorporators.

Miner v. Belle Isle Ice Co., 17 L. R. A. 412 (Mich.)

This has no resemblance to the case at bar. That was a case in which the dominating stockholder, with a bare majority of the stock, and by a long series of transactions definitely set up in the bill, had looted the corporation and had expended its profits, and had so managed the corporation that its business could not be carried on with profit to the stockholders. The record in that case showed fraud, bad faith, including a long series of illegal transactions, the absorption of all of the profits by the defendant Lorman, and the practical loss of the investment value of the interests of the minority stockholders. We have no such circumstances in the case at bar. On the contrary, it is admitted in the bill that under the management of Lathrop, with practically no investment at all, the corporate assets increased to an amount where the bulk of them were sold for $831,000.00, and after paying all corporate obligations there is a net profit of $600,000.00. The only items seriously questioned in the case at bar are credits to the president amounting to around $22,500.00, shortly subsequent to the sale which he negotiated at such a handsome profit to the corporation. It is admitted here that the majority

of this stock is owned by defendant Lathrop. In other words, aside from his other assets, it is admitted that he has assets of his own amounting to $300,000.00. What court of equity has ever granted a receiver, wound up the affairs of a corporation, and destroyed the corporation, because of some difference of opinion as to the matter of compensation of the president of the corporation? Defendant Lathrop has no objection at all to a friendly suit brought in the state court to determine the propriety of this extra compensation for the sale of this property. There is no court in the land, after hearing the history of this corporation, that will hold that the time and effort and business acumen devoted for years to the consummation of this sale, in addition to the usual duties of managing a water business, was not worth the amount awarded. But if the court should so hold, Lathrop is able, ready and willing to return the money to the treasury. The only method by which transactions can be had is through the board of directors. We have here the picture of Mr. Stillwell, an attorney at this bar, writing a letter of solicitation to a total stranger, and getting a contract out of him on a contingent fee basis; and without any authority from Swan in so far as this record discloses (Stillwell was upon the stand, and counsel for appellant was given an opportunity to make a full statement) filing this suit. It is a sad spectacle indeed to see Mr. Stillwell, a co-executor in the estate of Gridley, stirring up dissensions and attempting to wreck the corporation in which the estate of Gridley has an interest and which it is his sworn duty to preserve, coming into this court and seeking to invoke its assistance in his endeavor to liquidate the corporation so that he may receive a fee.

The decision in the Belle Isle Ice Co. case quotes with approval the language of Judge Wallace, in which he says:

> "It cannot be denied that minority stockholders are bound hand and foot to the majority in all matters of legitimate administration of the corporate affairs; and the courts are powerless to redress many forms of oppression, practiced upon the minority under a guise of legal sanction, which fall short of actual fraud."

This is a fair statement of the law. In the case at bar there is no oppression. In fact, none is charged in the bill. No *facts* are alleged which indicate oppression, much less actual fraud.

Minona Portland Cement Co., 167 Ala. 485.

It was conceded in this case that the allegations of the complaint were sufficient to entitle the plaintiff to dissolution under the laws of Alabama. The complaint alleged that the corporation was a failure; that the business for which it was formed could never be inaugurated or carried on, and the court held that under these circumstances, in view of the law of the state of Alabama, the plaintiffs were entitled to relief.

O'Connor v. Knoxville Hotel Co., 93 Tenn. 708, 28 S. W. 308.

In this case the court granted relief in view of the fact that the corporation complained of was organized to build a projected hotel at a cost of $200,000.00. $72,000.00 worth of stock had been subscribed. No action had been taken by the corporation for four years. Taxes and interest were eating up the capital already subscribed and

the population had moved away, making the building of the hotel impractical.

The court held that under these circumstances relief should be granted. There are no such allegations in the instant case.

Porter v. Industrial Information Co., 25 N. Y. Sup. 328.

This was another insolvency case. The court said:

"The application for the appointment of receiver seems to be warranted by Section 1810, Subdivision 3, of the code. The facts as gathered from the papers before me seem to be that the corporation is wholly insolvent, that it has defaulted in one law suit, and that another will come to judgment shortly."

Supreme Sitting etc. v. Baker, 134 Ind. 293.

This was also an insolvency case. The opinion of the court reads:

"It is alleged that appellees are informed and believe and, therefore, charge the fact to be, that the appellant corporation is now insolvent."

Thoroughgood v. Georgetown Water Co., 9 Del. Ch. 84.

In this case relief was refused, the court saying:

"As the case now stands, the chancellor does not feel that the resources and power of the directors have been exhausted to remedy the condition complained of."

Toledo v. Pennsylvania, 54 Fed. 746, holds that the federal court has jurisdiction "of the whole case" in a suit in equity praying that certain railroad companies be restrained from refusing to afford equal facilities to

the complainant, holding that "a court of equity has power to contrive new remedies and issue unprecedented orders to enforce rights secured by federal legislation, provided no illegal burdens are imposed thereby." (Syllabus.)

This authority would seem to indicate the concession on the part of the appellant that the remedy he is seeking is unprecedented, that he is endeavoring to establish here a new rule.

Towle v. American Bldg., Loan & Inv. Soc., 60 Fed. 132, cited by plaintiff, is also a case in which a receiver was appointed for an *insolvent* corporation. This distinguishes the case from the case at bar without further comment. The court makes pertinent references, however, to the matter of jurisdiction. It says:

> "A much more serious objection, however, is the one that the parties to the suit have been collusively arranged for the purpose of creating a case cognizable in the federal courts. It cannot be seriously disputed that, in the absence of collusion, a stockholder has a a right to bring his action against the corporation in the federal courts, provided diverse citizenship exists, and the case is one in which the stockholder is entitled to an action at all. * * *
>
> "So apparent already had the abuse become that Congress inserted in the act of March 3, 1875, the provision that if, at any time in the progress of the case, either originally commenced in the circuit court or removed there from the state court, it should appear that the suit did not really and substantially involve a dispute or controversy properly within the jurisdiction of the federal court, or that the parties to the suit had been improperly or collusively made or joined, either as plaintiffs or defendants,

for the purpose of creating a case cognizable or removable to the federal court, the court should proceed no further, but dismiss the suit peremptorily, or remand it to the state court.

"I conceive it to be the duty of the federal courts to examine each case carefully to ascertain if it falls within the terms of this provision. The jurisdiction of the state courts, and the application of state policy, ought not to be taken away, except in those cases which fall within the spirit of the judiciary act. The system of federal courts is not intended to supersede the state courts, but only to furnish a tribunal where the substantial rights of citizens of different states may be determined. To extend this jurisdiction further, so as to take in the controversies which are practically between the citizens of the same state, is to erect tribunals not contemplated, either by the Constitution of the United States or of the state, and contrary to the spirit of both. The fact of diverse citizenship of complainant and defendant, in such a case as this, is not, therefore, in my opinion, standing alone, a sufficient warranty to hold jurisdiction. In the absence of any good reason for bringing the action into the federal courts, I would be disposed to hold that the arrangement of the parties was collusive for jurisdictional purposes. The question then arises, is there any substantial reason why the shareholder, seeking an administration of these assets, should select the federal courts? And, if so, was it the reason that dominated the bringing of this action therein?"

We have no quarrel with the rule in other jurisdictions that where the purpose of the corporation has been fulfilled or has become impossible the courts of equity can interpose where it is absolutely necessary to do so.

The articles of incorporation of Consolidated Water Company are not set forth in the bill and it is not alleged what *all* of the purposes of the corporation are, nor is it alleged that *all* of the purposes of the corporation have been fulfilled or that they are impossible of fulfillment.

Town v. Duplex-Power Car Co., 172 Mich. 519, presents a state of facts entirely at variance with the allegations of the bill herein. In that case there was a "conspiracy to wreck the company." (In the case at bar the conspiracy to wreck the company is chargeable to the plaintiff and not to the defendants.) There were also two sets of directors, who "were each claiming to be lawful officers of defendant company." The court says:

> "Attention has been directed to the fact that the court below had before it more than a sworn bill and sworn answers. Upon the application for a receiver, the court was bound to consider whether, in view of all facts presented, there was reasonable prospect that the defendant company would be able to carry on its business and save its property; whether, however lawful the debt secured by mortgage of its assets may be, the security was given and its foreclosure was contemplated with the purpose on the part of the defendants to secure the property of the company for themselves; whether it was likely that with rival boards of directors contending for control of the company either could command business success; and, finally, whether the charges that defendants were conspiring to exclude and injure the complainants were not so well established by the correspondence produced and by other circumstances, that a receiver with the duty of preserving the property of the corporation ought to be appointed.

> "We express no opinion upon the merits, or apparent merits, of the controversy. We are of the opinion that the injunction granted was too broad, and should have been limited to restraining the trustees and all others interested from a foreclosure of the mortgage, upon condition, however, that complainants secure eventual payment of the debts secured by the mortgage, if found to be valid debts of the corporation. Likewise, the order appointing the receiver should have confined him to preservation merely of the assets of the corporation."

It will be noted that the action in the Town case was a creditors' bill, and that it came under the well established rule whereby, in the case of a deadlock in the board of directors or rival claims of office it becomes necessary to protect the assets on behalf of the creditors, the court may appoint a receiver. There are no such facts in the case at bar.

U. S. Shipbuilding Co. v. Conklin, 126 Fed. 132, merely holds that a receiver may be appointed to preserve the assets of an *insolvent* corporation. We have no quarrel with that rule. The same rule is laid down by Section 564, Subdivision 5, of the Code of Civil Procedure of California. There is no allegation in the bill herein that the defendant corporation is insolvent.

Zeckendorf v. Steinfeld, 225 U. S. 445.

This was an Arizona case, but the statutory provisions as to receivers in that state are not set out. However, the appointment of a receiver was apparently only sustained "in view of the situation of the property *and the final winding up of the company.*"

It clearly appears that the above cases fall in two classes, those where the corporation is alleged to be in-

solvent and those cases where it has ceased to function or the object is incapable of fulfillment.

Dissolution.

We come now to the question of dissolution. Many of the cases above cited refer to this subject, and plainly indicate that the bill of complaint does not state a cause of action for dissolution. The dissolution of a corporation is regulated by statute in California, and there is no power in the court to compel a dissolution, except in accordance with the provisions of the statute. There are only two methods provided by law for involuntary dissolution: One under Section 358 of the Civil Code, which in part reads as follows:

> "If a corporation does not organize and commence the transaction of its business, or the construction of its works within one year from the date of its incorporation, or if, after its organization and commencement of its business, it shall lose or dispose of all of its property, and shall fail for a period of two years to elect officers and transact, in regular order, the business of said corporation, its corporate powers shall cease, and the said corporation may be dissolved at the instance of any creditor of the said corporation, at the suit of the state, on the information of the attorney general, but the resumption of its business in good faith by such corporation prior to the commencement thereof shall be a bar to such suit,"

and the other under the provisions of Section 803, *et seq.*, of the Code of Civil Procedure. Section 803, C. C. P., reads as follows:

> "Action may be brought against any party usurping, etc., any office or franchise. An action may be

brought by the attorney general, in the name of the people of this state, upon his own information, or upon a complaint of a private party, against any person who usurps, intrudes into, or unlawfully holds or exercises any public office, civil or military, or any franchise, or against any corporation, either *de jure* or *de facto*, which usurps, intrudes into, or unlawfully holds or exercises any franchise, within this state. And the attorney general must bring the action, whenever he has reason to believe that any such office or franchise has been usurped, intruded into, or unlawfully held or exercised by any person, or when he is directed to do so by the governor. (Amendment approved 1907; Stats. 1907, p. 600.)"

It is obvious that the bill does not bring the case at bar within either of these sections.

Voluntary dissolution is provided for by Sections 1227-1235 of the Code of Civil Procedure. Sections 1227 and 1228, C. C. P., read as follows:

"Sec. 1227. CORPORATION, HOW DISSOLVED.—A corporation may be dissolved by the Superior Court of the county where its principal place of business is situated, upon its voluntary application for that purpose. (Amendment approved 1880; Code Amdts. 1880, p. 109.)

"Sec. 1228. APPLICATION FOR DISSOLUTION OF CORPORATION, WHAT TO CONTAIN.—The application must be in writing, and must set forth:

"1. That at a meeting of the stockholders or members called for that purpose, the dissolution of the corporation was resolved upon by a vote of two-thirds of the members or of the holders of two-thirds of the subscribed capital stock;

"2. That all claims and demands against the corporation have been satisfied and discharged. (Amendment approved 1907; Stats. 1907, p. 318.)"

In 7 Cal. Jur., at page 135, it is stated:

"The law provides for three methods of dissolution of a corporation, one by direct act of the Legislature, another by *quo warranto,* and a third by voluntary act of the corporation itself; and the rule is that a corporation can be dissolved only in the manner prescribed by statute. As the jurisdiction of the Superior Court to decree dissolution exists only by virtue of the statute, either at the suit of an individual or at the suit of the state, the court is limited by the provisions of the statute both as to the conditions under which a dissolution may be brought about, and as to the extent of the judgment which it may make in the exercise of this jurisdiction. A court cannot treat a corporation as already dissolved because its condition is such that it will be necessary or proper for it to institute proceedings for dissolution. And as ownership of property is not essential to the existence of a corporation, a transfer of all its property does not work a dissolution But if a corporation loses or disposes of all its property and fails for a period of two years to elect officers and transact, in regular order, its business, it may be dissolved at the instance of any creditor at the suit of the state, on the information of the attorney general."

It, therefore, conclusively appears that the bill stated no cause of action for dissolution and upon that ground should be dismissed.

Reply to the Summary of the Bill of Complaint, as Set Forth in Appellant's Opening Brief, Page 4.

(1) CHARGE OF "FRAUD":

We find no charge of fraud in the bill. Paragraph 10 of the bill sets up certain cancellation of indebtedness, and

the voting of certain sums to Lathrop and Gridley. The only allegation is that "neither said Lathrop nor Mrs. Gridley had rendered said corporation any services whatsoever to justify said payments." There is no allegation that there was no other consideration for these payments, and so far as appears by the bill, these payments were made for a valuable consideration of some sort other than services. In any event, it is not alleged that these payments were fraudulently made, or that they were not made in good faith. For instance, the payment of a salary of $250.00 per month to the president of a corporation that increased its assets from practically nothing to $600,000.00 would not seem to present any of the earmarks of a transaction which should occasion a court of equity to throw a corporation into the hands of a receiver, ruin its credit and wreck it, particularly in view of the fact that the president to whom the salary was paid has since died and left a goodly portion of her assets to the very people who, it appears from the testimony of Stillwell, are behind the scenes in this action.

The other transaction which is questioned by the appellant (and very indefinitely and inadequately questioned, as a matter of pleading), is that of a loan to Pacific Land and Cattle Company. There is no allegation that this loan was not for the benefit of Consolidated Water Company, or that the cattle company is insolvent, or that it is not amply able to answer an immediate call for its return; nor is there any allegation that any demand has ever been made by anybody that the loan be repaid. In the absence of such allegations, it must be presumed that this transaction was for the benefit of Consolidated

Water Company, and was not fraudulent. It must be presumed also that Pacific Land and Cattle Company is ready, willing and able to return the money. There is no allegation of fact in this bill indicating that the defendant corporation cannot continue to do business, that its profits have been absorbed, dissipated, or that the definite items in dispute cannot be litigated and determined in a proper action for that purpose.

It must be remembered that the board of directors of a corporation has discretion in the conduct of the business of the corporation.

Cal. Jur. Corporations, 528;

Fox v. Hale & Norcross Silver Mining Co., 108 Cal. 369, 426.

At most, the transactions are merely voidable and notice and demand on directors are prerequisite to suit. However, this is an action for receiver and dissolution and not an action to set these transactions aside.

This is not an action to compel the payment of dividends. If there is complaint that profits were reinvested in the business and that since the sale of the property dividends have not yet been distributed, plaintiff is at liberty to bring a suit to compel such dividends, but the allegations with respect to dividends have no place in this bill and state no cause of action.

Mulchay v. Hibernian Savings and Loan Society, 144 Cal. 219;

Zellerbach v. Allenburg, 99 Cal. 57.

Mismanagement:

As stated above, the salaries paid to the appellee Lathrop and to Mrs. Gridley were very modest in view of the admitted success of their efforts.

Betrayal of Trust in Refusal to Vote Stock of the Gridley Estate as the Interests of the Owners, the Legatees, Required and as They Demanded:

Of course, it would have done no good for these shares to have been voted as demanded, as it clearly appears that the demanders did not own two-thirds of the stock of the corporation, and in view of the allegations of the bill, that there were but five thousand shares of stock, of which Lathrop and his associates are conceded to have owned at least 2397½ shares, it is quite obvious that the two-thirds vote, required under section 1228 of the Code of Civil Procedure of California for voluntary dissolution, could not have been obtained, regardless of how Lathrop voted the stock in question. Therefore, his refusal was immaterial. Of course, as an executor he had the legal right to use his own judgment as to what was or what was not to the interests of the estate. The legatees were not stockholders of record, and had no voice in the matter.

(2) Sale oe corporate assets.

There are allegations concerning the sale of the water plant at Pomona. While under the law of this state, as hereinafter set forth, it would make no difference, it is apparently the theory of the plaintiff that this plant having been sold the corporation should be dissolved. It appears from the allegations in the bill that the stockholders of Consolidated Water Company originally had a very small investment and that under the management of appellee G. A. Lathrop the assets of the corporation grew to the amount of eight hundred thousand dollars (Complaint, Par. VIII), and that the profits were in ex-

cess of fifty thousand dollars per annum. It can be reasonably inferred from the growth of assets that the profits of the concern were reinvested in extensions and improvements, in pumping plants and pipe lines—the usual course of affairs in a growing community. However, regardless of these facts, the contention of plaintiff falls of its own weight. It is difficult to determine whether or not the plaintiff is complaining of the sale of this property for eight hundred thousand dollars. We do not see how he can complain of it and ask the court to affirm it by distributing the results thereof to the stockholders. Some mention is made that the stockholders of the company were not asked to approve the sale, the theory being that the approval was required under Sec. 361-a of the Civil Code. Before answering this contention let us remark that Sec. 361-a of the Civil Code refers only to the transfer of "business, franchise and property, as a *whole.*" Now assuming that this was a purported transfer of all the property as a whole and the approval of the stockholders had not been had, the transfer would have been void. In other words there would have been no transfer and the proper action of the plaintiff would be a stockholders bill joining the city of Pomona in a suit to declare the transfer void and tendering to the city of Pomona the return of the consideration paid to Consolidated Water Company. Section 361-a of the Civil Code provides:

> "361-a. Transfer of franchise of corporation not valid without consent of stockholders. No sale, lease, assignment, transfer or conveyance of the business, franchise and property, *as a whole,* of any corporation now existing, or hereafter to be formed in this state, shall be valid without the consent of stockholders thereof, holding of record at least two-

> thirds of the issued capital stock of such corporation; such consent to be either expressed in writing, executed and acknowledged by such stockholders, and attached to such sale, lease, assignment, transfer or conveyance, or by vote at a stockholders' meeting of such corporation called for that purpose; but with such assent, so expressed, such sale, lease, assignment, transfer, or conveyance shall be valid; *provided, however, that nothing herein contained shall be construed to limit the power of the directors of such corporation to make sales, leases, assignments, transfers or conveyances of corporate property other than those hereinabove* set forth."

There is no allegation in the bill that the property transferred to the city of Pomona was all of the property of the corporation and all of its franchises and right to do business. Indeed the contrary appears. Paragraph XIV limits the action of the Board of Directors to that "employed and used in furnishing water to the inhabitants of San Jose Township and vicinity and to the inhabitants of the city of Pomona", and paragraph XV refers to an application to the Railroad Commission "to sell the water system, rights, plant, business and *substantially* all of the property of said corporation to the city of Pomona." In the same paragraph is set out the title to the Railroad Commission application, confining the matter to "its water system."

Paragraph XVI referring to bills of sales and conveyances to the city of Pomona confines the property transferred to that "employed in furnishing water as aforesaid" and to the "working capital and assets of said corporation, whereby it *carried on said water business.*" Similar references are contained in paragraphs XVII and XVIII

of the bill. The bill is careful not to say that the business, franchise and property *as a whole* have been disposed of, and it affirmatively appears that if there were an attempt to dispose of the business, franchise and property as a whole it would be an abortive attempt, because, as alleged in the bill, the stockholders have not approved any such transaction and therefore the corporation would still own the property and it would be incumbent upon the Board of Directors to continue the conduct of the business. The fact is plainly inferred by the bill that there are other property and other rights belonging to this corporation and the corporation must continue to exist for the purpose of handling and conducting them.

Dial v. Homestead Land Co., 39 Cal. App. 480;
Thompson on Corporations, 3rd Ed. Sec. 4562;
C. C. 361;
Bradford v. Sunset Land Co., 30 Cal. App. 87.

(3) THE PURPOSE FOR WHICH THE CORPORATION WAS FORMED HAS BEEN ACCOMPLISHED.

There is no allegation in the bill that the furnishing of water is or was the *sole* purpose of the corporation. And counsel very well know that no such allegation can be incorporated in the bill. If the sale to the city of Pomona had included all of the corporation assets, it would have been void according to the law of this state. The fact that not all of the assets but a *portion* of them admittedly was sold (a sale which, under the laws of California, this California corporation had a right to consummate), makes the transaction legal, and the approval of the stockholders was not required. It seems, however, that appellant is perfectly willing to ratify this

sale by asking that a portion of the proceeds be paid to him. Under these conditions, he cannot be heard to utilize such transaction as ground for receiver, dissolution or other intervention of a court of equity. It is not alleged that this sale was an unprofitable one; on the contrary, it crystallized the profits of the corporation into a gain of $600,000.00, admittedly under the skill and management of Lathrop. If appellant is to treat this sale as void, then his remedy is to join the city of Pomona as a defendant in an action to compel a redelivery of the property and a repayment to the city of Pomona of the $831,000.00 received. But plaintiff is careful not to reflect upon the propriety of this sale as a business transaction negotiated by Lathrop for the benefit of the corporation and its stockholders. Of course, appellant and the other stockholders represented by counsel, aggregating all told less than three per cent. in stock ownership, do not want to void this sale. They challenge it merely in an unfair endeavor to put Lathrop, the man who created this entire valuation, in the wrong upon some technicality. If in good faith they wanted to challenge this transaction they could have done so by a suit in which the city of Pomona was joined. It was certainly as easy to bring that suit as this one.

Paragraph XI is entirely too general, and a court of equity should not be compelled to reach out its arm and take the burden of investigation of this kind in view of the fact that any stockholder has the right to examine the books. A stockholder should not unnecessarily demand the interposition of courts of equity. Before putting this burden upon the time of the court and the already overburdened judicial machinery, the stockholder should

at least examine the books and see what he can find out himself and make his allegations accordingly. There is no statement in the bill that the appellant has personally or through an agent looked over the books of the corporation and that he had discovered certain facts upon which he bases the bill, or for reasons stated was unable to discover the facts. (Civil Code, Sections 377, 378.)

(4) That defendant Lathrop is attempting to embark the corporation in a new and different line of business.

In view of the fact that there is no allegation in the complaint that the sole purpose of the corporation was to supply the city of Pomona with water, it cannot be contended that the appellee Lathrop is embarking in a new and different line of business not contemplated by the stockholders. The allegation that there was an intention to change the purposes of the corporation states no cause of action and has no bearing upon any purported cause of action.

Under section 362 of the Civil Code, a corporation has the right to amend its articles as to purposes. This section provides:

> "Amendment of articles of incorporation. Amended articles filed with secretary of state. Any corporation organized under the laws of this state may amend its articles of incorporation for any or all of the following purposes:
>
> (1) * * *
>
> (2) To alter or repeal any provision appearing in its original or amended articles of incorporation relative to the purposes for which the corporation is

formed, or to set forth additional powers or purposes.

(3) * * * " *etc.*

(5) THE PLAINTIFF HAS DEMANDED OF APPELLEES THAT STEPS BE TAKEN TO WIND UP THE CORPORATION.

The allegation in the complaint has to do with the efforts made in behalf of appellant by Mr. Austin to obtain a voluntary dissolution of the corporation. These efforts were unavailing and have no place in this bill, and have no bearing upon an action brought for involuntary dissolution.

(6) THAT THE CORPORATION IS NOT BEING MANAGED OPERATED OR CONTROLLED IN THE INTERESTS OR FOR THE BENEFIT OF THE STOCKHOLDERS.

The history of this corporation, as alleged in the bill, shows that starting with almost nothing the profits were accumulated and reinvested and preserved for the stockholders.

The assets of the corporation, as admitted by the appellants, amount to more than $600,000.00.

In conclusion, we quote the summing up of the holdings of the Federal Courts by Judge Morris of the District of Delaware in the case of Myers v. Occidental Oil Corporation, 288 Fed. 997, 1003.

> "Moreover, it must be observed that judicial statements to the effect that a receivership may properly be constituted, although the legitimate purposes of a corporation may not have become impossible of accomplishment, if the facts clearly disclose *such fraudulent, willful or reckless mismanagement* of its business and affairs by its board of directors as to

produce a conviction that further control of the corporation by the same board would result in the *destruction of its business and insolvency,* or cause great and unnecessary loss to its creditors or stockholders, but made in suits in which receivership is not the primary object, as in United States Shipbuilding Co. v. Conklin, *supra,* and Carson v. Allegany Window Glass Co. (C. C.) 189 Fed. 791, 796, are not authority in support of the contention that receivers may be so appointed without regard to the nature or ultimate object of the suit in which receivers are sought."

* * * * * * * * *

"If, however, this court is without power in this suit to sell and distribute the corporate assets, receivers may not be appointed to aid in so doing. That this court has such power in receiverships under the Delaware statute is clear. Jones v. Mutual Fidelity Co. (C. C.) 123 Fed. 506; Carson v. Allegany Window Glass Co. (C. C.) 189 Fed. 791. But, the allegation of insolvency not having been established, the statutory power is not here available. The great weight of authority is to the effect that its inherent jurisdiction does not enable a court of equity, at the instance of a stockholder, to dissolve or wind up a corporation by the sale and distribution of all its assets, because of the mismanagement or fraud of its officers and stockholders. 39 L. R. A. (N. S.) 1032, note. In Vila v. Grand Island E. D. I. & C. S. Co., 68 Neb. 222, 97 N. W. 613, 110 Am. St. Rep. 400, 4 Ann. Cas. 59, an ably considered case, the court, quoting from Wallace v. Pierce-Wallace Pub. Co., 101 Iowa, 313, 70 N. W. 216, 38 L. R. A. 122, 63 Am. St. Rep. 389, said:

'It is certainly true that, in the absence of express statutory authority, jurisdiction of courts of

> equity does not exist over corporate bodies to such an extent as to justify them in dissolving corporations or in winding up their affairs and sequestrating their property. This seems to be so well settled that there is scarcely a dissenting voice in authority.' "

There is an enlightening note in *L. R. A. New Series, Vol. 39, at p. 1032, et seq.* We will not quote this note at length but under the heading "I. General Rule," the following statement is made:

> "The general rule has been asserted that corporations are the creatures of the state, hence, in general, their life depends upon the action of the state or the stockholders as a whole; and especially if a going concern whose charter or franchise has not yet expired, they cannot, in the absence of statute, be dissolved at the instance of a stockholder by an action in equity for that purpose, and therefore equity is without jurisdiction of a suit by a stockholder, the principal purpose of which is to wind up the affairs of the corporation or to have a receiver appointed with that end in view."

The authorities as indicated by this note are overwhelmingly against the position of plaintiff in this suit and plaintiff's endeavors to bring itself within the confines of some exception is obviously unsupported by the facts alleged, by any principle of equity or by any appropriate authority.

We submit that courts do not look with favor upon complaints emanating from stockholders representing an infinitesimal percentage of the stock who apparently have not even taken the trouble to have access to the books of the corporation, who have not attempted any adjustment or arbitration of difficulties out of court in

so far as the transactions of the officers of the corporation are concerned, and who come into court at the instigation of one who has no interest in the corporation other than sharing in a fee for wrecking it. There is no doubt of the general rule as shown by cases which we have cited that where the conduct of the directors or their failure to act is such that the corporation is at a standstill and cannot function as such, the courts of equity will interpose and preserve the assets when absolutely necessary to do so.

There is no such situation in this case. On the contrary, the defendants desire to proceed and to conduct the business of the corporation and to keep it alive, and the assets are in no wise endangered. There is no insolvency either on the part of the corporation or of G. A. Lathrop. Far from it. Nor is there any creditor whose rights are sought to be preserved, nor is there any inaction on the part of the directors.

The plaintiff merely appears as a stockholder prosecuting a stockholder's bill for the benefit of the corporation. Under the authorities, assuming the facts to be as alleged in the bill, the plaintiff should have brought an action against Lathrop to compel restitution to the corporation of misappropriated funds. Instead, plaintiff predicates his cause of action upon an alleged right to compel the dissolution of the corporation. This being so, the case comes directly within the case of Cashman v. Amador, *supra*. In the Cashman case, Cashman appeared as plaintiff for the benefit of the county. In the case at bar, Swan appears as plaintiff for the benefit of the corporation. Cashman was not entitled to personal relief in that case; Swan is not entitled to personal relief

in this case. Therefore, this plaintiff has no right to have his cause of action adjudicated in this court.

Under the authorities cited, it is clear that the decree of the District Court, dismissing the Bill of Complaint herein "upon the ground that there is insufficiency of fact to constitute a valid cause of action in equity" was proper and should be affirmed.

Respectfully submitted,

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